



U.S. Department
of Transportation

Federal Highway
Administration

Memorandum

Washington, D.C. 20590

Subject: Equipment Rental Rates

Date **AUG 22 1986**

From: Director, Office of Highway Operations

Reply to
Attn of HHO-32

To: Regional Federal Highway Administrators
Regions 1-10

A recent OIG audit of construction equipment usage/rental rates used by State highway agencies (SHA's) for extra contract work has found that a significant number of the SHA's need to modify their rate schedules in order to meet Federal cost principles. Contractors in these States are being reimbursed for equipment usage based on predetermined rates which contain ineligible costs.

Federal policy requires that actual costs be used to determine extra work payments. However, since actual equipment costs are not readily available, the Federal Highway Administration (FHWA) has permitted SHA's to specify in their construction contract specifications the use of predetermined rate guides. The OIG has determined that for the most part these predetermined rate guides which include industry rate guides such as: "The Rental Rate Blue Book for Construction Equipment" (Blue Book); "The Rental Rate Blue Book for Older Construction Equipment" (Older Blue Book); "Construction Equipment Rental Rate Compilation" and the "Construction Equipment Ownership and Operating Expense Schedule" as well as equipment rate schedules developed by SHA's based on industry publications contain cost allowances which are ineligible for Federal reimbursement.

Ineligible cost allowances result from the use of contingency factors and replacement cost escalation factors. Contingency factors are unallowable under Office of Management and Budget (OMB) Circular A-87, Attachment B, Part D-2, "Standards for Selected Items of Cost." Inclusion of replacement cost escalation factors when computing depreciation likewise is not allowable. The OMB Circular A-87, Attachment B, Section B11 states: "the computation of depreciation or use allowance will be based on acquisition costs. Where actual cost records have not been maintained, a reasonable estimate of the original acquisition cost may be used in the computation."

The "Construction Equipment Ownership and Operating Expenses Schedule" published by the U.S. Army Corps of Engineers has been identified by the OIG as being an acceptable source of equipment usage rates without modification. Other predetermined rate guides may be considered as alternative guides if their

cost formulas and rate factors are identifiable and can be modified to adjust for unallowable and unreasonable costs. Rates should be adjusted to ensure that contingency factors are not included and that depreciation is computed over the estimated useful life of the equipment.

Please take the necessary steps to assure that predetermined equipment usage/rental rates used by the SHA's within your region comply with Federal cost principles. The SHA's which use the Blue Book and other rate methods should modify the equipment rates before they are applied to Federal-aid projects.


for David S. Gendell